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C O N F I D E N T I A L SECTION 01 OF 08 BANGKOK 003354

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DEPARTMENT PASS USTR FOR BWEISEL AND JJENSEN
COMMERCE FOR JBENDER AND JKELLY

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TAGS: ETRD EINV ECON TH
SUBJECT: DELAY IN FTA TALKS LIKELY TO HIT US EXPORTS

Classified By: Economic Counselor Michael J. Delaney. Reason: 1.4 b an
d d

¶1. (C) Summary. There is a growing possibility that US-Thailand Free Trade Agreement (FTA) negotiations will be indefinitely postponed. The sizable opportunity costs for US commerce of the FTA's failure have been documented in several econometric studies of the FTA's likely effects: foregone US exports are estimated to total around US$390 million per year, or US$3.9 billion over a 10-year period. Less well recognized is the likely cost to US commerce caused by trade diversion to non-US suppliers that have already negotiated much lower tariffs into the Thai market. Thailand has already finalized (or, we believe, soon will finalize) FTAs with some of its key trading partners, so an indefinite postponement of the FTA with the US will place a substantial percentage of our existing trade with Thailand at a double-digit tariff disadvantage -- US suppliers will face average effective tariffs of 16 percent for agricultural products, and 23 percent for industrial products, versus mostly zero tariffs for our competitors. About 75 percent of current US exports to Thailand overlap with products covered by Thailand's FTAs with other countries. Based on 2005 volumes and value, we estimate US$60.5 billion in US agricultural and industrial exports over the next ten years will be at risk due to trade diversion to FTA-covered suppliers from Japan, China, Australia, and New Zealand.

¶2. (C) There is evidence that FTA-induced trade diversion away from US suppliers is already occurring, and is likely to worsen over the next few years as Thailand's FTAs with our competitors are fully implemented. End Summary.

FTA Talks Could Be Delayed Indefinitely

¶3. (C) Thailand's political stalemate continues. The Thai courts have ruled that the April 2 elections were not constitutional, so the previous government remains in caretaker status. New elections eventually will have to be held, but apparently not until mid-October owing to continued legal and political wrangling. Thus, the current state of political limbo will through 2006, making the resumption of FTA talks with the US ever more problematic given the US's own scheduling constraints (TPA expiration, resources requirements of other FTAs). Further lengthening the odds of successful conclusion of the FTA is the reality that, at least in the short term, any future Thai government may shy away from re-engaging on the FTA. The FTA is politically controversial and unpopular here, and may be relegated to the

"too hard" category by an incoming (possibly fragile) government.

¶4. (C) Commerce Vice Minister Uttama Savanaya (who is Deputy Prime Minister and Commerce Minister Somkid's personal representative in the FTA talks) told us recently that he does not believe a future government would be in a position to undertake any major policy initiatives in the short term, including the resumption of FTA negotiations. Minister Somkid himself on May 26 told the Ambassador that while he is anxious to resume FTA negotiations once an elected government is in place (Somkid estimated that a government could be formed by December 2006), he warned that FTA talks "cannot resume along the same lines as before." Although he did not provide details, we believe Somkid is prepared to negotiate a narrow, market access for goods FTA modeled (we believe) on Thailand's FTA with Japan. The FTA would be "phased," with most non-tariff issues being left for later. (Comment: Somkid's and Uttama's latest comments are consistent with what they have been saying for some time. Somkid is in favor of market liberalization in principle, but has since 2004 confided to other Thai Government officials his doubts that Thailand could accommodate the US requirement for a comprehensive FTA Somkid's lack of enthusiasm for the FTA left PM Thaksin as its only strong Thai proponent, and played a role in the subsequent problems the FTA talks encountered. Somkid probably calculates that a comprehensive, US-style FTA is more than the fragile Thai political system can handle right now. End Comment.)

Opportunity Costs Under a No-FTA Scenario

¶5. (C) Given the current politics and attitudes here,

combined with US scheduling and resources constraints, there is a growing possibility that there will be no comprehensive US-Thailand FTA for the foreseeable future. We have examined how this "No FTA" scenario would affect future US exports to Thailand, as well as Thai exports to the US. In a sense, such a calculation has already been done in the several econometric studies of the effects of an FTA on bilateral trade volumes and GDP growth. (See, for example, the USITC's "US-Thailand Free Trade Agreement: Advice Concerning the Probable Economic Effects of Providing Duty-Free Treatment for Imports:, dated August 2004; and the Thai Development Research Institute's "A Study on the Impacts of a Thailand-US Free Trade Agreement", dated October 9, 2003.) These studies typically take as a baseline the existing trade regimes of the two economies, and calculate the trade effects of full market liberalization, i.e., the elimination of all tariffs and most non-tariff barriers. The result of that calculation of "baseline trade flow versus trade flow under a liberalized, post-FTA regime" is the economic benefit of the FTA (the result can be readily converted into annual GDP growth, employment generation, or other measurements). Conversely, that same result would be the "opportunity cost" of not having an FTA. According to these econometric studies, these opportunity costs would be commercially significant: the FTA would boost US GDP by about 0.1 percent over a ten-year period (US$11.75 billion), and boost US exports to Thailand by about 4.7 percent annually (i.e., US$390 million per year, or US$3.9 billion over a 10-year period).

Trade Diversion Effects Under a No-FTA Scenario

¶6. (C) Less well documented is the likely damage to existing bilateral trade if the FTA is indefinitely postponed. If we want to know the true cost to US commerce of an indefinite delay of our current FTA initiative with Thailand, earlier econometric analyses are incomplete since the existing bilateral trade regime -- the "baseline" -- is changing in important ways that are likely to cause trade diversion from US exports. Trade diversion effects are relatively high for Thailand because Thailand's MFN tariffs

are relatively high. In the absence of an FTA with the US, Thailand's FTAs with other countries will place at risk most (about 75 percent) existing US exports to Thailand. Perhaps the most important change for US exporters is Thailand's current or imminent implementation of FTAs with Australia, New Zealand, China, and Japan. FTAs with Australia and China have been signed and are already in effect; the FTA with Japan has been finalized and awaits signing.

¶7. (C) In general, Thailand's non-US FTAs cover market access, particularly tariff reduction/elimination, for varying product (goods) categories. In most cases, the FTA-covered product tariffs go to zero after a phase-in period. That will give these countries a significant price advantage over the US, since Thailand's current effective MFN tariffs average about 16 percent for agricultural products and 23 percent for industrial products. Over time, trade diversion to these lower tariff suppliers is likely.

Future US Services Investments Could Also Be Negatively Impacted

¶8. (C) Under the US-Thailand Treaty of Amity and Economic Relations (AER), US investors enjoy preferential, better-than-MFN treatment for a range of services investments in Thailand. Thailand's 10-year GATS derogation permitting this arrangement expired in January 2005. AER rights currently are being extended by 90-day intervals pending successful completion of the FTA. The perception that Thailand's FTA negotiations with the US are on more or less indefinite hold would increase pressure on Thailand to withdraw benefits to US investors that are provided under the AER.

¶9. (C) Thailand's exports to the US also face uncertainties. The implementation of CAFTA and other FTAs poses a competitive threat. Another question mark is the future of the US Generalized System of Preferences (GSP). Thailand currently is the third-biggest beneficiary of the GSP, with about one-third (more than $5 billion worth) of Thailand's exports to the US enjoying GSP tariff-free

treatment. With the current GSP program scheduled to expire at the end of 2006, some US policymakers have expressed the desire to revamp the program, spreading out the benefits to more countries and focusing more on the least developed economies, that is, away from a middle income country like Thailand.

Thailand's FTA with Australia

¶10. (C) The Thailand-Australia FTA (TAFTA) entered into force on January 1, 2005. The agreement focuses on market access, particularly tariff reduction. Thailand will phase out its tariffs on some 2,934 tariff items, around 53 percent of all items, accounting for 78 percent of current Thai imports from Australia. Of these, only 206 items were previously duty free. A further 41 percent of Thai tariffs will be phased to zero by 2010. These items cover 17 percent of current trade. All remaining tariffs, including tariff rate quotas, will phase to zero in 2015 or 2020 (with the exception of skim milk powder and liquid milk and cream, for which the tariff rate quotas will be eliminated in 2025).

Agricultural Products

¶11. (C) For agricultural products subject to tariff rate quotas prior to January 1, 2005, Thailand has either eliminated the tariff and quota restrictions or will expand access for Australia over a transition period varying according to the product, before final elimination of the tariff rate quota.

¶12. (C) Meat -- Thailand will phase the current 32% tariff for sheep meat to zero in 2010. Thailand immediately reduced

the tariff on beef to 40 percent, down from 51 percent, and for beef offal to 30 percent, down from 33 percent, and will phase these rates to zero in 2020. Thailand will phase the current 33 percent tariff for pork to zero in 2020. (Note: The cited pre-FTA tariff rates are applied on an MFN basis and, as such, are the tariff rates applied to US imports.)

¶13. (C) Dairy -- Thailand immediately eliminated the previous tariffs on infant formula (5 percent), lactose (up to 2 percent), casein and milk albumin (10 percent), and will phase the tariffs on butter fat, milkfood, yoghurt, dairy spreads and ice cream to zero in 2010. The FTA provided an immediate additional quota for Australia of 2,200 tons for skim milk powder and 120 tons for liquid milk and cream, expanding by 17 percent at five-yearly intervals until 2025, when all tariffs and quotas will be eliminated. It will phase the tariffs for butter and cheese, other milk powders and concentrates to zero in 2020.

¶14. (C) Grains and related products -- Thailand immediately eliminated the previous tariffs on wheat (ad valorem equivalent of 12-20 percent), barley, rye and oats (ad valorem equivalents of up to 25 percent), and the tariff and tariff rate quota on rice. It also immediately eliminated the tariffs on unroasted malt (ad valorem equivalent of 28 percent) and wheat gluten (31 percent), and will phase the tariffs on wheat flour (32.6 percent) and starch (31 percent) to zero in 2010.

¶15. (C) Fruit and Vegetables -- Thailand will phase tariffs on most fresh fruit and vegetables (current rates mostly 33 percent or 42 percent) to zero in 2010. Tariffs on mandarins (42 percent) and grapes (33 percent) were immediately reduced to 30 percent, and will be phased to zero in 2015. Thailand immediately eliminated its tariffs on most tropical fruit, and provided immediate additional quota for fresh potatoes, expanding yearly until 2020, when all tariffs and quotas will be eliminated. The current 30 percent tariffs for processed potatoes will be phased to zero in 2015.

¶16. (C) Thailand immediately reduced to 24 percent the previous tariffs of 30 percent on fruit juices and canned fruit, and will phase the tariff to zero in 2010. The previous 30 percent tariffs on canned mixed fruit and canned pineapple were eliminated immediately.

¶17. (C) Sugar -- Thailand provided immediate additional quota for sugar, expanding annually by 10 percent, with

tariff and quota free access in 2020.

¶18. (C) Wine, Beer and Spirits -- Thailand immediately reduced its previous 54 percent tariffs on wine to 40 percent, and will phase the tariff to zero in 2015. For beer and spirits, Thailand immediately reduced its previous tariffs of 60 percent to 30 percent, before phasing to zero in 2010.

¶19. (C) Other Processed Foods -- Thailand immediately eliminated its previous 10 percent tariffs on chocolate confectionery, and will phase its current 30 percent tariff on sugar confectionery to zero in 2010. For bakery products, Thailand will mostly phase current tariffs of 25-30 percent to zero in 2010, with immediate elimination of tariffs on crispbread and some cereals.

¶20. (C) Other Agricultural Products -- Thailand immediately eliminated its previous tariffs of up to 10 percent on hides and skins. Thailand immediately eliminated its previous 1 percent tariff on wool and will bind its tariff on cotton at zero.

Industrial Products

¶21. (C) On entry into force, Thailand reduced tariffs on any industrial goods not subject to immediate elimination to a ceiling of no more than 20 percent (with the exception of small and medium passenger motor vehicles), before phasing to zero. (Pre-FTA industrial effective tariff rates average about 23 percent.) Where not eliminated immediately, tariffs on a range of industrial goods identified by Australia as of specific interest were halved immediately before phasing to zero.

¶22. (C) Motor Vehicles and Components -- Thailand immediately eliminated tariffs on large passenger motor vehicles (engine capacity of over 3000cc) and goods vehicles, previously at 80 percent and 60 percent respectively. For other passenger motor vehicles, Thailand immediately reduced the previous 80 percent tariff to 30 percent, before phasing this down by 6 percent each year to zero in 2010. Tariffs on all automotive parts, components and accessories, previously up to 42 percent, were immediately reduced to a ceiling of 20 percent, and will be phased to zero by 2010. Tariffs on engines were immediately reduced from the previous 30 percent to 15 percent. Other tariffs previously at or below 20 percent were also immediately reduced and phased down accordingly.

¶23. (C) Machinery and Equipment -- Prior to January 1, 2005, Thai tariffs ranged up to 30 percent. Tariffs were either immediately eliminated or will be phased to zero by 2010, with the exception of three tariffs covering electric power boards, which will be eliminated in 2015. Tariffs of 20 percent for electric transformers and inductors were eliminated immediately. Tariffs of 30 percent for fully-automatic washing machines and combined refrigerator-freezers were eliminated immediately.

¶24. (C) Steel -- Thailand immediately eliminated its 1 percent tariff on slab steel. Thailand immediately halved its tariffs on flat-rolled steel products of interest to Australia, including hot-rolled coil (previous tariff of 10 percent), cold-rolled coil (12 percent) and coated steel (15 percent). Tariffs will then be eliminated in 2015, with the exception of most coated steel products for which the tariffs will be phased to zero in 2008.

¶25. (C) On long steel products, Thailand will generally reduce tariffs to zero by 2010. On a limited number of products, including structural sections and merchant bar, Thailand immediately halved tariffs, which will then be held until elimination in 2015. On steel articles, where Thailand's previous tariffs were generally 20 percent, Thailand eliminated some tariffs immediately, with the remainder to be phased to zero by 2010.

¶26. (C) Non-ferrous metals -- On unwrought copper cathode, Thailand will eliminate the tariff in 2010, prior to that Thailand will bind the rate at no more than 5 percent, and will apply a tariff of no higher than the rate applied to its

ASEAN partners. On copper bars and pipes, with previous tariffs of 10 percent, Thailand either eliminated the tariff immediately or reduced it immediately to 5 percent and will eliminate it in 2007. On aluminum bar, sheet and foil, with previous tariffs of 10 percent, Thailand reduced immediately to 5 percent the tariff on items of specific interest and will eliminate it in 2007, while remaining tariffs will phase to zero in 2009. Thailand immediately eliminated its 1 percent tariff on unwrought aluminum. On unwrought lead and zinc, with previous tariffs of 10 percent, Thailand either eliminated the tariff immediately or reduced the tariff immediately to 5 percent and will eliminate it in 2007.

¶27. (C) Pharmaceuticals -- Thailand will phase current tariffs of 10 percent or 20 percent to zero in 2009. On products of specific interest, previous tariffs of 10 percent were halved immediately and will be eliminated in 2007.

¶28. (C) Fertilizers -- Thailand immediately eliminated previous fertilizer tariffs at 5 percent, and immediately halved previous tariffs of 10 percent before elimination in
¶2007.

¶29. (C) Photographic Goods -- Thailand immediately eliminated tariffs of 20 percent on photographic film, paper and chemicals.

¶30. (C) Plastics -- Thailand immediately reduced tariffs of 30 percent on plastic articles to 20 percent and will phase to zero in 2010. For the most significant item of current trade, miscellaneous plastic articles, not separately identified in the tariff schedule, Thailand immediately eliminated the previous 30 percent tariff. Thailand will phase the current tariffs of up to 20 percent on polymers to 5 percent in 2008 and to zero in 2010.

¶31. (C) Other Goods -- Thailand immediately eliminated the previous tariff of 10 percent on golf club parts; immediately eliminated the previous tariff of 20 percent on parts of seats; immediately eliminated the previous tariff of 20 percent on ferries under 1,000 tons, and will bind the current zero tariff on ferries of over 1,000 tons.

Thailand's FTA with New Zealand

¶32. (C) Thailand's FTA with New Zealand is similar in key respects to that of Australia's. New Zealand is a major supplier of dairy products and meat to Thailand. Trade diversion away from US suppliers to New Zealand competitors is likely to occur, but will be mitigated by supply constraints in New Zealand.

Thailand's FTA with China

¶33. (C) Thailand's FTA with China is fairly narrow, focusing on reciprocal "early harvest" tariff reductions in a limited range of agricultural products. Starting in 2004, tariffs are phased to zero by 2006 for the following products: live animals (Thailand's current applied MFN tariff rate is 10.5 percent); meat and edible meat offal (35.4 percent); fish and crustaceans (5 percent); dairy products (23.3 percent); products of animal origins (12.5 percent); live trees and other plants (33.2 percent); edible vegetables, roots, and tubers (35.4 percent); and edible fruits and nuts (32.4 percent).

Likely Trade Diversion Costs for US Exporters by Sector

¶34. (C) Fruit -- China,s fruit exports have surged since the signing of the Sino-Thai zero-for-zero accord covering fruits and vegetables. Fortunately for US suppliers, total market size increased and US net exports were not displaced (for now). Imports from China have been on the upswing over the past five years, rising from US$19 million in 2000 up to US$63 million in 2005. Meanwhile, US exports have been flat at around US$18 million annually for the past five years. Australia and New Zealand started off with about US$4 million (combined) five years ago and are now up to US$7 million in 2005, just prior to the kick-off of their FTA-mandated reduced tariffs. Combined competitive pressure from China, Australia and New Zealand could reduce the competitiveness of US fruit in this market. Currency devaluation, however,

might discount US fruit enough to offset this. Unfortunately, freight disadvantage for US products will be exacerbated by high fuel costs, perhaps trumping both currency values and tariff offsets.

¶35. (C) We project that US fruit exports to Thailand will taper off as Australia and New Zealand displace US apples, cherries, peaches, plums, and berries. US exports will fall by about US$3 million in 2007, and another US$1 - 2 million

in 2008.

¶36. (C) Nuts -- Australia,s nut exports to Thailand have boomed since 2001, jumping from less than US$100,000 then to over US$600,000 in 2005. Tariff reductions and high quality from Australia will only further increase the competitiveness of Australian tree nuts (as opposed to ground nuts). China will, of course, elbow the US out of some business; the question is just how much. US nut exports to Thailand were very strong up to 2005, racking up some $8 million that year. Given the substitutability of U.S. nuts by Australian ones, look for US nut exports to suffer, probably coming down half a million annually, as long as Australia has the supply.

¶37. (C) Wine -- US market share in Thailand has dropped steadily over recent years. Australia tops the list of suppliers, providing plentiful supplies, affordable prices, reasonable quality, and low shipping costs. New Zealand is creeping up the ranks, showing that it can pull in over 1 percent of the market with its tiny exports and high demand for its quality wines in higher purchasing power markets. Look for the paltry US$150,000 exports of US wine to Thailand to stay flat. Any growth in the market will fall to the Australians or Europeans.

¶38. (C) Beef -- Thailand is a tiny beef market, buying less than US$5 million annually from all sources. The unfortunate find of BSE in the US meant that American beef exports collapsed in 2004 and 2005. New Zealand and Argentina took up most of the slack (Australia was topped out and could not muster the export muscle.) The US is currently battling back to regain market share in Thailand. Tariff disadvantages compared to antipodean origin meat will only serve to make the comeback more difficult. It is hard to isolated losses in the meat market due solely to BSE (mad cow) or to price / tariff disadvantages, but either way, US beef is headed for a protracted fight in Thailand. The best-case scenario is that US beef makes it way back to US$1 million annually. Australia, New Zealand, and Argentina will take the lion,s share. Without negative tariff pressure caused by the FTAs with Australia and New Zealand, US beef would easily regain it former position in the market.

¶39. (C) Dairy Products -- New Zealand has grown its presence in the Thai market through aggressive marketing and attractive prices. Australia is right on their heels. The US has recently become competitive due mostly to domestic pricing restructuring. This segment of the market is particularly price conscious, given that quality and availabilities are largely the same from the major suppliers. More so than in other product categories, tariff reductions on Southern Hemisphere dairy products ought to play out in higher export numbers, too. Look for US losses in this category, possibly as much as US$5 million a year due to lower tariffs for Australian and New Zealand suppliers.

¶40. (C) Pet Food -- Of the US$20 million or so in pet food that enters Thailand annually, over half comes from Australia. The US has held steady at just over 30 percent of the market. Many US manufacturers have production facilities in Australia and will easily be able to shift resources to Australia to follow the demand from markets like Thailand. Look for direct and proportional market losses as tariffs drop for Australian and New Zealand suppliers.

¶41. (C) Hides and Skins -- This is a huge market segment for the US, racking up some US$50 to US$75 million annually. Closely related to the beef slaughter industry, hides and skin exports to Asia (Thailand, Philippines, and Korea) have been very strong due mainly to strong supplies and stable, attractive prices. With very few quality differences among suppliers, it is reasonable to assume that Australia and New Zealand will be able to erode the US share as tariffs on

their product decline. In 2005, US exports were about US$55

million compared to the combined Australia/NZ volume of about US$45 million.

¶42. (C) Thailand imports around US$2.8 billion in food and agricultural products annually. To this can be added a few more tens of millions for lumber and fiber. The US has been the leading supplier of agricultural products to Thailand, sending in around half a billion worth of products in 2005. Australia is rising in importance as a supplier, reaching the number 5 position with about US$200 million in exports to Thailand that same year.

¶43. (C) Much of the US export power in the Thai market is due to dominance in soybean, wheat and cotton trade) areas where Australia cannot erode the US position or where the FTA will not provide any incentive to switch from US to Aussie supply. The US vulnerability comes in the areas beyond farm commodities in their &pure8 sense. The US vulnerability is in product categories where tariffs are higher, and where reasonable substitutes are available (processed food products, semi-finished foods like frozen French fries, consumer ready products such as juices, cereals, as well as the perishable and high cost products like fruits, vegetables, etc.)

¶44. (C) If one were to take the so-called bulk commodities out of the US mix, that would leave about half of the value in value-added and consumer ready products, that area most vulnerable to Aussie (and other FTA) erosion. Of these approximately US$250 million &at risk8 exports, look for a gradual wearing away of the US numbers as tariff preference shifts to our Southern competitors. The deterioration of market share will likely be accelerated due to rapidly rising freight costs, too (with Australia and NZ enjoying relative freight advantages over the US). Therefore, we believe the value of US agricultural exports to Thailand will shrink continually over the next decade, losing perhaps as much as half of their current value due to lack of competitiveness.

Thailand's FTA With Japan: Focus is on Industrial Goods

¶45. (C) Thailand's FTA with Japan poses the biggest threat to US exports of industrial goods. The FTA with Japan has been finalized, but remains unsigned. Thai officials have told us that they regard the signing of the FTA with Japan as fairly likely in the near future, notwithstanding the current political impasse in Thailand. Their optimism derives from the recognition that unlike the FTA with the US, the FTA with Japan has been completed and only needs to be signed. Furthermore, it has not attracted the same popular attention and controversy as has the FTA with the US (probably because it focuses almost exclusively on non-agricultural tariffs). The FTA text is not publicly available. However, Japanese diplomats in Bangkok have told us that the FTA is heavily oriented toward phased reduction/elimination of tariffs on industrial goods. We believe the FTA text calls for implementation (including phased tariff reduction and elimination upon full FTA implementation) to begin January
¶2007.

¶46. (C) Thailand's MFN effective tariffs for manufactured goods currently average about 23 percent. The US and Japan are direct competitors across a range of products in the Thai market: of the top twenty categories of US exports to Thailand, eleven are also included in the top 20 list of Japanese exports to Thailand. The categories in which the US competes directly with Japan comprise better than 78 percent of total US exports to Thailand. Upon full implementation, Japanese industrial goods are likely to face de minimus tariffs, while US goods will face the average effective tariff rate of 23 percent. As the FTA's tariffs are phased in (in most cases to zero), US products will gradually lose their price competitiveness against substitutable Japanese products.

Total Value of US Exports At Risk Due to FTA-Induced Trade Diversion

¶47. (C) The twin effects of agricultural product trade diversion from Australia/New Zealand/China, and industrial product trade diversion from Japan, is likely to severely

impact US exports to Thailand. Once these FTAs are fully implemented, US exporters will have to overcome a double-digit tariff disadvantage. The lack of an FTA with Thailand would put at risk at least US$1.25 billion (based on 2005 values and volumes) in US agricultural exports over the next ten years. Upon full implementation of the FTA with Japan, we estimate that about US$59 billion (based on 2005 values and volumes) in US industrial exports over the next ten years to Thailand will be at risk. Thus, about $60.5 billion (based on 2005 values and volumes), or about 75 percent of total US exports to Thailand, will be at risk once all of Thailand's FTAs are fully implemented.

Trade Diversion Is Already Happening

¶48. (C) We use the relatively moderate term "at risk" to characterize the impact on US suppliers, since it is impossible to gauge the precise impact of differential tariffs on US exports. Many issues besides differential tariffs are at play, including availability of supply, quality, cost and reliability of delivery, and proprietary technology. It is likely that the effects of the US's tariff disadvantage will vary from product to product.

¶49. (C) In terms of overall US exports to Thailand, will tariff discrimination matter? Based on our examination of preliminary data, the answer is an emphatic "Yes." FTA-mandated reduction in tariff rates is already having a big impact on Thailand's import mix, skewing it toward FTA countries. According to full-year Thai statistics, Australian exports to Thailand grew by 47 percent in 2005, compared to the US exports' growth of only 20 percent. Gold and crude petroleum were the main contributors, but Australian exports of wheat, aluminum, copper, zinc, lead, automotive engines and parts, malt, dairy products, electrical machinery and equipment, fruit and nuts, pet food and pharmaceuticals also grew strongly.

¶50. (C) US exports of cereal (the 14th largest US export to Thailand, HS code 10) increased 27 percent in 2005 compared to the previous year, whereas Australia's increased 57 percent. US exports of pharmaceuticals (the 18th largest category of US exports to Thailand) increased 17.9 percent in 2005 compared to 2004, whereas Australian exports increased 31.1 in the same period. Articles of iron and steel (HS code 73) was the 9th largest US export to Thailand by value in 2005 increasing 13.8 percent over 2004. Australia's exports to Thailand in this category increased 90.3 percent over the same period. These results are particularly troubling given that Australia's FTA with Australia has not been fully implemented; 2005 was only the first year of the FTA's multi-year tariff phase-out schedule, i.e., tariffs for the most part have not yet phased to zero. It could be that that the worst is yet to come as the Australia versus US tariff gap in the Thai market widens.

¶51. (C) Since the Thailand-Japan FTA has not been signed or implemented, there is no hard data on how this FTA might affect US exports. We note, however, that since Thailand's effective tariff rates for industrial goods is higher than its effective agricultural tariff rates (16 percent versus 23 percent), the trade diversion effect (in this case, away from US suppliers, to Japanese suppliers) on US exports may be greater than what we have seen for agricultural products with the Australia FTA.

Conclusion

¶52. (C) The available import statistics present an incomplete picture, and we are working with the American Chamber of Commerce in Thailand to gain a fuller, more

detailed understanding of the likely impact on US exporters of Thailand's FTAs with our competitors. But we already have enough information to confidently project that the combination of implementation of these FTAs and inaction on the US FTA is likely to severely damage our overall competitiveness in the Thai market, resulting in the loss of a significant share of our current exports to Thailand.

BOYCE